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No. 351

In the Supreme Court of the United States

OCTOBER TERM, 1958

THE BROWN PAPER MILL COMPANY, INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT

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INDEX

	Page
Opinions below	1
Jurisdiction	1
Questions presented	1
Statutes involved	2
Statement	3
Argument	6
Conclusion	18

CITATIONS

Cases:

Arkansas Motor Coaches v. *Commissioner*, 198 F. 2d 189 11

Bradford Machine Tool Corp. v. *Commissioner*, decided October 29, 1958 10

Central Paper Co. v. *Commissioner*, 199 F. 2d 902 11

Colonial Amusement Co. v. *Commissioner*, 173 F. 2d 568 10

Colorado Milling & El. Co. v. *Commissioner*, 205 F. 2d 551 10

Commissioner v. *Blue Diamond Coal Co.*, 230 F. 2d 312 11

Commissioner v. *S. Frieder & Sons Co.*, 228 F. 2d 478 11

Commissioner v. *Seminole Mfg. Co.*, 233 F. 2d 395 11

Corn Products Refining Co. v. *Commissioner*, 215 F. 2d 513, certiorari denied on this question 348 U. S. 911, affirmed on other issues, 350 U. S. 46 10

Crowell-Collier Publishing Co. v. *Commissioner*, decided October 7, 1958, petition for writ of certiorari pending, No. 500, this Term .. 10, 11, 13

Cases—Continued

	Page
Dayton Rubber Co. v. *Commissioner*, 249 F. 2d 2	10
Dowd-Feder, Inc. v. *Commissioner*, 173 F. 2d 673	10
Frank, A. B., Co. v. *Commissioner*, 211 F. 2d 497	10
Helms Bakeries v. *Commissioner*, 236 F. 2d 3	11, 13, 14, 15, 16
Helms Bakeries v. *Commissioner*, 28 T. C. 79, appeal pending (No. 15,574, C. A. 9)	13, 19
Kemp, George, Real Estate Co. v. *Commissioner*, 182 F. 2d 847, certiorari denied, 340 U. S. 852	10, 16
Kemp, George, Real Estate Co. v. *Commissioner*, 205 F. 2d 236	11
Packer Publishing Co. v. *Commissioner*, 211 F. 2d 612	11
Patent Button Co. v. *Commissioner*, 256 F. 2d 726	10, 13
Standard Hosiery Mills v. *Commissioner*, 249 F. 2d 469	10, 16
Stimson Mill Co. v. *Commissioner*, 163 F. 2d 269, certiorari denied, 332 U. S. 824	10
United States v. *California Eastern Line*, 348 U. S. 351	9
United States v. *Koppers Co.*, 348 U. S. 254	10
Washington v. *Miller*, 235 U. S. 422	17
Waters, James F., Inc. v. *Commissioner*, 160 F. 2d 596, certiorari denied, 332 U. S. 767	10, 12, 14

Statutes and Regulations:

Administrative Procedure Act, § 10, 60 Stat. 237 (5 U. S. C. 1009)	18
Excess Profits Tax Act of 1940, 54 Stat. 975 (as amended, 26 U. S. C. (1952 ed.) 710 *et seq.*)	6
Excess Profits Tax Act of 1950, 64 Stat. 1137, (26 U. S. C. (1952 ed.) 430 *et seq.*)	13

Statutes and Regulations—Continued

	Page
Internal Revenue Code of 1939 (26 U. S. C. (1952 ed.)):	
§ 430 *et seq*	13
§ 710 *et seq*	6
§ 711 (b)	7
§ 714	7
§ 721	7, 8
§ 722	7, 8, 9, 11, 17
§ 722 (b)	4, 5
§ 722 (d)	5, 8, 9, 17
§ 732	2, 17
§ 732 (a)	2, 8, 17
§ 732 (b)	3
§ 732 (c)	3, 6, 8, 9, 10
§ 732 (d)	3, 8
§ 1141	16
Internal Revenue Code of 1954 (26 U. S. C. (Supp. V)):	
§ 7482	15, 16
§ 7851 (a) (6) (C)	15, 16
§ 7851 (a) (7)	15, 16
Renegotiation Act of 1942, § 403 (e) (1), 56 Stat. 245, as amended (50 U. S. C. App. 1191 (e) (1))	9
Revenue Act of 1945, 59 Stat. 556	16
Treasury Regulations 109, § 30.722–5 (a)	5
Miscellaneous:	
H. Rep. No. 146, 77th Cong., 1st Sess	9
H. Rep. No. 1337, 83d Cong., 2d Sess	16
H. Rep. No. 2333, 77th Cong., 2d Sess	10
S. Rep. No. 75, 77th Cong., 1st Sess	9–10
S. Rep. No. 1622, 83d Cong., 2d Sess	16
S. Rep. No. 1631, 77th Cong., 2d Sess	10

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OPINIONS BELOW

The opinion of the Tax Court (R. 16–158) is reported at 23 T. C. 47. The opinion of the court of appeals (Pet. 1a–7a) is reported at 255 F. 2d 77.

JURISDICTION

The judgment of the court of appeals was entered on May 8, 1958. A timely petition for rehearing was denied on June 11, 1958. The petition for a writ of certiorari was filed on September 9, 1958. The jurisdiction of this Court is invoked under 28 U. S. C. 1254 (1).

QUESTIONS PRESENTED

1. Whether the ultimate findings of fact made by the Tax Court in denying excess profits tax relief

under § 722 of the Internal Revenue Code of 1939 may be reviewed by the court of appeals for alleged inconsistency or lack of evidentiary findings, notwithstanding the provision of § 732 (c) of the Code that the Tax Court's determination of any question made "necessary solely by reason of * * * section 722 * * * shall not be reviewed or redetermined by any court."

2. Whether the Tax Court's denial of such relief because the claim was not adequately presented to the Commissioner within the time prescribed by the regulations may be reviewed by the court of appeals.

STATUTES INVOLVED

Section 732 of the Internal Revenue Code of 1939, 55 Stat. 17 (as amended, 26 U. S. C. (1952 ed.) 732):

> SEC. 732. REVIEW OF ABNORMALITIES BY THE TAX COURT OF THE UNITED STATES.
>
> (a) *Petition to the Tax Court.*—If a claim for refund of tax under this subchapter for any taxable year is disallowed in whole or in part by the Commissioner, and the disallowance relates to the application of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, relating to abnormalities, the Commissioner shall send notice of such disallowance to the taxpayer by registered mail. Within ninety days after such notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the ninetieth day) the taxpayer may file a petition with The Tax Court of the United States for a redetermination of the tax under this subchapter. If such petition is so filed, such notice of disallowance shall be deemed to be a notice of deficiency for all purposes relating to the assessment and

collection of taxes or the refund or credit of overpayments.

(b) *Deficiency Found by the Tax Court in Case of Claim.*—If the Tax Court finds that there is no overpayment of tax in respect of any taxable year in respect of which the Commissioner has disallowed, in whole or in part, a claim for refund described in subsection (a) and the Tax Court further finds that there is a deficiency for such year, the Tax Court shall have jurisdiction to determine the amount of such deficiency, and such amount shall, when the decision of the Tax Court becomes final, be assessed and shall be paid upon notice and demand from the collector.

(c) *Finality of Determination.*—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question shall not be reviewed or redetermined by any court or agency except the Tax Court.

(d) *Review by Special Division of the Tax Court.*—The determinations and redeterminations by any division of the Tax Court involving any question arising under section 721 (a) (2) (C) or section 722 with respect to any taxable year shall be reviewed by a special division of the Tax Court which shall be constituted by the presiding judge and consist of not less than three judges of the Tax Court. The decisions of such special division shall not be reviewable by the Tax Court, and shall be deemed decisions of the Tax Court.

STATEMENT

Petitioner filed with the Commissioner applications for relief under § 722 of the Internal Revenue Code of

1939[1] as to excess profits taxes paid for the years 1940–1945. (The nature of the relief authorized by § 722 is indicated in the introductory paragraphs of the Argument, *infra*, pp. 6–8.) The Commissioner denied the claims for relief. On taxpayer's petition for redetermination, the Tax Court held as follows with respect to the § 722 relief claims relevant here:

(1) Taxpayer claimed that its industry (manufacture of kraft paper) was temporarily depressed during the base period (1936–1939) because of a temporary over-expansion of capacity in the industry. The Tax Court found as a fact that the growth in the number of mills during that period was "not unusual, but was about normal" and that neither petitioner's business nor the industry was depressed "because of any temporary economic event or circumstance, unusual in its history or that of its industry" (R. 128), and accordingly denied any relief on that ground (R. 141–145).

(2) In its application for relief filed with the Commissioner for 1940, petitioner claimed relief under § 722 (b) (4) for a "change in the character of the business" during the base period, but did not indicate the nature of the change. Section 722 (b) (4) defines that phrase as including a change in operation or management, a change in products or services, a change in capacity for production or operation, a change in the ratio of borrowed capital to total capital, or the acquisition of a competitor. In the Tax Court, petitioner claimed that there had been a change

[1] Unless otherwise indicated, section references are to the 1939 Code.

in the ratio of its borrowed capital to its total capital. The Tax Court, while granting relief on that ground for years for which it had been timely asserted (1941–1945), denied relief for 1940 because that basis for relief had not been specified in the application filed with the Commissioner, as required by the regulations under § 722 (R. 134–137).[2]

(3) In the Tax Court petitioner claimed an increased capacity for production during the base period by reason of the installation of "McDonald dehydrators". The applications for relief filed with the Commissioner had asserted only, without specification, a "change in the character of the business" under § 722 (b) (4). The Tax Court denied relief on this ground because it was not timely asserted (R. 148), although it did take the new dehydrators into account in allowing a reconstruction of base period net income on the ground of a change in petitioner's method of operation (R. 148–149).

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[2] Section 722 (d) requires application for relief to be made to the Commissioner "in accordance with regulations prescribed by the Commissioner." The regulations under that section in effect when the application was filed (Sept. 1943, R. 134) required such applications to be filed within the time prescribed for claims for refund and provided:

> * * * the application for relief shall set forth in detail and under oath each ground under section 722 upon which the claim for relief is based, and facts sufficient to apprise the Commissioner of the exact basis thereof. The mere statement of the provision or provisions of law under section 722 upon which the claim for relief is based shall not constitute an application for relief within the meaning of section 722. (Regs. 109, § 30.722–5 (a)).

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(4) Petitioner also claimed an increased capacity for production by reason of the installation of "Sutherland refiners". The Tax Court found as a fact that these new machines, while more cheaply performing one phase of production, did not increase the plant's capacity for production of the final product and denied the relief sought on that ground (R. 128, 145–148). The new refiners were, however, taken into account in allowing a reconstruction of base period net income on the ground of a change of method of operation (R. 148–149).

On petition for review to the court of appeals, petitioner alleged that the Tax Court's ultimate conclusions on the above issues were inconsistent with, or unsupported by, its evidentiary findings and that its holding that some of the claims were not timely and adequately presented to the Commissioner was erroneous. The court of appeals held that each of these contentions related to determinations made "necessary solely by reason of * * * section 722" within the meaning of § 732 (c) of the Code and hence were not reviewable by the court of appeals (Pet. 5a–7a). It also held that § 732 (c) of the 1939 Code had not, as petitioner claimed, been repealed by the 1954 Code (Pet. 3a–5a). Accordingly, the court dismissed the petition for review without reaching the merits.

ARGUMENT

The Excess Profits Tax Act of 1940 (§§ 710 *et seq.* of the Internal Revenue Code of 1939) was designed to recover in taxes excessive profits arising out of wartime conditions. It imposed a very high rate of tax on corporations on their profits in excess of a

norm (the "excess profits credit") representing the taxpayer's "normal" profits. In general, the "excess profits credit" was based on the taxpayer's average profits during the presumably "normal" period of 1936–1939 (the "average base period net income").[3]

The difference between a taxpayer's income during the "base period" and its income during the war years might often, of course, be due to factors other than wartime conditions and thus not provide a fair measure of its excessive profits. To afford relief from the resulting inequities, three kinds of special adjustments (in addition to all others) were authorized: Section 711 (b) (1) (H–K) permitted "abnormal" deductions during the base period to be eliminated in determining the average base period net income. Section 721 permitted "abnormal" items of income realized in the excess profits tax year but attributable to other years to be reallocated to such years. Section 722, the section directly involved here, was a general relief provision available when the taxpayer could show that its average base period net income was "an inadequate standard of normal earnings" because of various enumerated factors causing base period earnings to be less than "normal"—such as unusual interruptions of production, economic circumstances peculiar to the taxpayer or its industry, newness of the business, or a change in the character or capacity of the business during the base period. If the inadequacy of the average base period net income was thus

[3] An optional method of computing the excess profits credit as a percentage of the taxpayer's "invested capital" (§ 714) is not involved here.

established, a "fair and just amount representing normal earnings" would be determined and used as a "constructive" average base period net income for purposes of arriving at the excess profits credit.

Because of the immense complexity of the issues raised by claims for relief under these so-called "relief" or "abnormality" provisions and the unique character of the relief they authorized, the Act established a specialized procedure for determination of such claims. With one limited exception, the taxpayer was required to pay the full tax without regard to its claim for relief under § 722 and then seek relief by a claim for refund (§ 722 (d)). Disallowance of the refund claim by the Commissioner was made reviewable upon a petition to the Tax Court (which normally has jurisdiction only over asserted deficiencies and not over claims for refund) (§ 732 (a)). In the interests of greater expertise and uniformity even within the Tax Court itself, a "special division" of at least three judges was to review the decisions of other divisions (typically, single judges) on § 722 and §721 (a) (2) (C) claims. The decisions of the Special Division, in turn, were not to be reviewed by the full Tax Court (§ 732 (d)). Finally, § 732 (c) provided:

> *Finality of Determination.*—If in the determination of the tax liability under this subchapter the determination of any question is necessary solely by reason of section 711 (b) (1) (H), (I), (J), or (K), section 721, or section 722, the determination of such question

shall not be reviewed or redetermined by any court or agency except the Tax Court.

The sole issue in this case is whether the review sought by petitioner in the court of appeals was precluded by this provision.[4]

1. (a) The claims for relief involved here—based on an alleged temporary depression in the industry due to an over-expansion of capacity, a change in the ratio of petitioner's borrowed capital to its total capital, and a change in petitioner's capacity for production—were all grounded solely on § 722. The Tax Court found that some of the grounds for relief asserted were not supported by the evidence and denied relief on others because they were not presented to the Commissioner in the time and manner prescribed by the regulations under § 722 (d). Inasmuch as all of these questions, whether of fact or of law, related solely and exclusively to petitioner's claims for relief under § 722, it would seem indisputable that, as the court of appeals held, appellate review was barred by § 732 (c).[5]

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[4] The lack of any similarity between the wording of § 732 (c) and that of the Renegotiation Act of 1942 fully distinguishes the issue here from that in cases arising under that Act. The Renegotiation Act gave the Tax Court "exclusive jurisdiction, by order, to finally determine the amount, if any, of such excessive profits" from renegotiable contracts. § 403 (e) (1), 56 Stat. 245, as amended, 50 U. S. C. App. 1191 (e) (1). The Court held in *United States* v. *California Eastern Line*, 348 U. S. 351, that a determination whether a particular contract was "renegotiable" was not a determination of the "amount" of excessive profits and hence was reviewable.

[5] That that was the intended scope and effect of § 732 (c) was made unmistakably clear by the committee reports. H. Rep. No. 146, 77th Cong., 1st Sess., pp. 14–15; S. Rep. No. 75, 77th

Section 732 (c) has been consistently applied by at least six courts of appeals to bar appellate review of questions of the sort sought to be presented by petitioner.[6] That section has been held to be inapplicable, on the other hand, only in cases presenting questions of an entirely different kind: (1) questions deemed to turn on other provisions of law in addition to the relief provisions (so-called "combination questions");[7] (2)

Cong., 1st Sess., pp. 15–16; H. Rep. No. 2333, 77th Cong., 2d Sess., p. 149; S. Rep. No. 1631, 77th Cong., 2d Sess., pp. 206–207.

Since § 722 is a relief provision granted as a matter of legislative grace, there can be no question of the constitutionality of denying appellate review of the Tax Court's decision. See Pet. 3a; *James F. Waters, Inc.* v. *Commissioner*, 160 F. 2d 596 (C. A. 9), certiorari denied, 332 U. S. 767; *Standard Hosiery Mills* v. *Commissioner*, 249 F. 2d 469 (C. A. 4).

[6] *Crowell-Collier Pub. Co.* v. *Commissioner*, 1958 P-H Fed. Tax Rep. ¶58–5229 (C. A. 2, Oct. 7, 1958), petition for writ of certiorari pending, No. 500, this Term; *Corn Products Refining Co.* v. *Commissioner*, 215 F. 2d 513 (C. A. 2) (§ 721), certiorari denied on this question, 348 U. S. 911, affirmed on other issues, 350 U. S. 46; *George Kemp Real Estate Co.* v. *Commissioner*, 182 F. 2d 847 (C. A. 2), certiorari denied, 340 U. S. 852; *Colonial Amusement Co.* v. *Commissioner*, 173 F. 2d 568 (C. A. 3) (§ 711 (b) (1) (J) and (K)); *Standard Hosiery Mills* v. *Commissioner*, 249 F. 2d 469 (C. A. 4); *A. B. Frank Co.* v. *Commissioner*, 211 F. 2d 497 (C. A. 5); *Bradford Machine Tool Corp.* v. *Commissioner*, 1958 P-H Fed. Tax Rep. ¶58–5278 (C. A. 6, Oct. 29, 1958); *Patent Button Co.* v. *Commissioner*, 256 F. 2d 726 (C. A. 6); *Colorado Milling & El. Co.* v. *Commissioner*, 205 F. 2d 551 (C. A. 10) (§ 711 (b) (1)). See also *United States* v. *Koppers Co.*, 348 U. S. 254, 267–269 (dictum).

[7] *Stimson Mill Co.* v. *Commissioner*, 163 F. 2d 269 (C. A. 9), certiorari denied, 332 U. S. 824; *Dowd-Feder, Inc.* v. *Commissioner*, 173 F. 2d 673 (C. A. 6); *Dayton Rubber Co.* v. *Commissioner*, 249 F. 2d 2 (C. A. 6). See *Crowell-Collier Pub. Co.* v. *Commissioner*, *supra*; *Colorado Milling & El. Co.* v. *Commissioner*, *supra*, at p. 552; *George Kemp Real Estate Co.* v. *Commissioner*, *supra*, at p. 849.

questions going to the Tax Court's jurisdiction, such as the timeliness of the petition to the Tax Court;[8] (3) questions of res judicata;[9] and (4) questions whether issues independent of the right to relief (so-called "standard issues," such as the allowability of deductions) could be raised in a relief proceeding.[10]

(b) The sole divergence from the otherwise consistent pattern of decisions is the decision of the Ninth Circuit in *Helms Bakeries* v. *Commissioner*, 236 F. 2d 3, set forth in the petition at pp. 8a–17a. In that case the taxpayer sought review of the Tax Court's denial of two claims for relief under § 722: one, a claim that its base period earnings had been depressed by a price war, and the other, a claim that there had been an increase in its capacity for production and operation during and at the end of the base period. The court

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[8] *Arkansas Motor Coaches* v. *Commissioner*, 198 F. 2d 189 (C. A. 8); *Central Paper Co.* v. *Commissioner*, 199 F. 2d 902 (C. A. 6). Cf. *Packer Pub. Co.* v. *Commissioner*, 211 F. 2d 612 (C. A. 8), where the Tax Court had refused to pass on a § 711 (b) (1) (J) claim apparently on the ground that it had not been timely raised in the Tax Court proceedings.

[9] *George Kemp Real Estate Co.* v. *Commissioner*, 205 F. 2d 236 (C. A. 2). Since the rationale of that decision was that the question of collateral estoppel turned on provisions of law other than § 722, while the issues here turn solely on the findings of fact made for purposes of § 722 and on the regulations issued specifically under that section (as to adequacy and timeliness of the administrative claims for relief), petitioner's suggestion of a conflict (Pet. 12–13) seems unfounded.

[10] *Commissioner* v. *Blue Diamond Coal Co.*, 230 F. 2d 312 (C. A. 6); *Commissioner* v. *S. Frieder & Sons Co.*, 228 F. 2d 478 (C. A. 3); *Commissioner* v. *Seminole Mfg. Co.*, 233 F. 2d 395 (C. A. 5). See *Crowell-Collier Pub. Co.* v. *Commissioner*, *supra*.

of appeals, consistently with the above cases and its own prior decision in *James F. Waters, Inc.* v. *Commissioner*, 160 F. 2d 596, certiorari denied, 332 U. S. 767, dismissed the appeal as to the first claim on the ground that § 732 (c) barred review. At the same time, however, it undertook to review and reverse the Tax Court's decision on the second claim, holding that the Tax Court's ultimate finding was inconsistent with its evidentiary findings and also that it had failed to make a further finding deemed pertinent by the court of appeals. The distinction between the court of appeals' action on the two claims apparently turned on the fact that an "inconsistency" or lack of findings was alleged only as to the second claim. The opinion does not disclose, however, why § 732 (c) was thought to be any less effective to foreclose review of that alleged error than of any other."

After remand of the *Helms* case, the Tax Court made further findings and reaffirmed its original denial

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"Although the jurisdictional issue was fully argued, the court's only reference to the issue in ruling on the second claim was (Pet. 16a–17a):

> In view of the evidentiary findings of the Tax Court on this subject, its conclusion "lack of productive capacity was not a factor which to any appreciable extent limited petitioner's sales" appears to be arbitrary and contrary to its own findings.
>
> * * * * * *
>
> In light of the foregoing record in respect to relief sought by the petitioner under Section 722 (b) (4), we are not precluded from assuming jurisdiction because of the provisions of Section 732 (c).

of relief, 28 T. C. 79. The decision was again appealed to the Ninth Circuit. Counsel for the Government, both in brief and in oral argument, urged the court to reconsider and overrule its decision in *Helms* and, accordingly, to dismiss the second appeal for lack of jurisdiction. Oral argument was heard on July 11, 1958. The decision has not yet been announced.

(c) Petitioner in this case, seeking to bring itself within the apparent "exception" to nonreviewability adopted in the *Helms* case, alleged in the court of appeals that the Tax Court's ultimate findings were inconsistent with its evidentiary findings. Nevertheless, the court of appeals—like two others faced with similar claims based on the *Helms* case [12]—refused to review the findings for insufficiency or inconsistency and dismissed the appeal under § 732 (c). There is at the present time, therefore, a seemingly square conflict of decisions on this point among the courts of appeals.

The excess profits tax imposed by the 1940 Act was in effect only until December 31, 1945 (except for the effect of a one-year carryback), and the 1950 Excess Profits Tax Act (64 Stat. 1137, 26 U. S. C. (1952 ed.) 430 *et seq.*) contained no provisions comparable to §§ 722 and 732 (c). It is also true that, in numbers at least, the great bulk of the relief claims under the

[12] *Patent Button Co.* v. *Commissioner*, 256 F. 2d 726 (C. A. 6); *Crowell-Collier Pub. Co.* v. *Commissioner*, 1958 P-H Fed. Tax Rep. ¶ 58-5229 (C. A. 2, Oct. 7, 1958), petition for writ of certiorari pending, No. 500, this Term.

1940 Act have already been finally processed. Nevertheless, it must be admitted that the question is one of substantial and continuing importance.[13]

(d) For the foregoing reasons, the Commissioner would not oppose the granting of certiorari to resolve a subsisting conflict with the decision of the Ninth Circuit in the *Helms* case. As noted above, however, the *Helms* case is now back before the Ninth Circuit to review the additional findings made by the Tax Court on remand, and the court has been asked to overrule its earlier decision. Since that decision was reached without explanation or analysis of § 732 (c), is inconsistent with the Ninth Circuit's own prior decision in *James F. Waters, Inc.*, v. *Commissioner, supra,* and the decisions of at least six other courts of ap-

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[13] At the present time, there are approximately fifteen cases involving the so-called "relief" provisions in the courts of appeals.

In the Tax Court, according to the latest available statistics, as of October 31, 1958, there were pending at various stages 175 cases (asserting relief in an aggregate amount in excess of $524,000,000) involving substantive issues under § 722 alone—in addition to an undetermined number of cases involving issues as to timeliness or adequacy of claims for § 722 relief, and other related issues. Further, it is reasonably estimated that there are between 50 and 75 cases in the Tax Court involving relief under § 721 or § 711 (b) (1) (H–K) aggregating at least $100,000,000, and possibly several times that amount.

We are also informed that there is an undetermined number of claims for relief under §§ 722, 721, or parts of 711 (b) (1) pending at various administrative stages in the Internal Revenue Service.

peals, and has been rejected by the three courts of appeals in which similar claims of "inconsistent findings" have been made since the *Helms* decision, there is at least a reasonable prospect that the court will itself disavow its earlier decision and thus resolve the apparent conflict. Should that occur there would, we submit, be no further reason for this Court to review the decision in this case.

In view of the possibility of a resolution of the conflict, the Court may wish to defer action on the petition in this case until the decision of the Ninth Circuit on the second appeal in the *Helms* case (which, as indicated above, was argued on July 11, 1958) has been announced. If so, the Court may further deem it appropriate, in order to forestall any possibility of the Ninth Circuit's awaiting the action of this Court, to enter an order noting that the case has been continued pending the decision in the *Helms* case.

2. The other contentions of petitioner are without merit and present no conflict or other occasion for review by this Court.

(a) Petitioner contends that § 732 (c) of the 1939 Code was repealed by § 7851 (a) (6) (C) and (a) (7) of the 1954 Code, and that judicial review of Tax Court proceedings in excess profits tax cases is now governed solely by the provisions of § 7482 of the 1954 Code (which makes Tax Court decisions subject to the same review as decisions of district courts in civil actions tried without a jury) (Pet. 14–16). The contention was fully answered by the court below (Pet. 3a–5a) and has been expressly rejected by two other

courts of appeals,[14] while at least two more have, without question, applied § 732 (c) to appeals taken after the adoption of the 1954 Code.[15]

Section 7482 of the 1954 Code, the general provision governing review of Tax Court decisions, was a substantially verbatim re-enactment of the § 1141 of the 1939 Code. See H. Rep. No. 1337, 83d Cong., 2d Sess., p. A434; S. Rep. No. 1622, 83d Cong., 2d Sess., p. 614. The provision in § 7851 (a) (6) (C) of the 1954 Code (part of the general "effective date" provisions) that the general administrative provisions there enumerated (one being the chapter governing judicial proceedings) should apply to taxes imposed under the 1939 Code can be read to mean no more than that those provisions were to be effective immediately to supersede their *counterparts* in the 1939 Code. See H. Rep. No. 1337, *supra,* at A442–A443. Section 7851 (a) (7), in turn, was simply a catch-all provision to assure the repeal of any provisions of the 1939 Code that had not been specifically provided for. Since the Excess Profits Tax Act of 1940 had already been specifically repealed in its entirety by the Revenue Act of 1945 (59 Stat. 556) as to years subsequent to 1945, and remained in effect only for purposes of proceedings involving the prior years, there was no need to deal with the Act at all and the omission of any reference to § 732 (c) in the 1954 Code

[14] See note 12, *supra.* See also *George Kemp Real Estate Co.* v. *Commissioner*, 182 F. 2d 847 (C. A. 2), certiorari denied, 340 U. S. 852, rejecting a similar contention based upon an amendment to § 1141 of the 1939 Code.

[15] *Helms Bakeries* v. *Commissioner*, *supra*; *Standard Hosiery Mills* v. *Commissioner*, 249 F. 2d 469 (C. A. 4).

seems quite without significance. In all events, repeals by implication are not favored (see *e. g., Washington v. Miller,* 235 U. S. 422, 428), and it cannot reasonably be inferred that Congress, without comment, intended by these general provisions to abandon the specialized procedure it had carefully established to deal with the unique problems presented by excess profits tax relief claims. And the fact that there was pending contemporaneously with the enactment of the 1954 Code a special bill, which failed of passage, to alter the procedure in relief cases (Pet. 15) proves, if anything, that the general provisions of the Code were not intended to have that effect.

Moreover, petitioner's contention that § 732 of the 1939 Code was "repealed" by the 1954 Code, if valid, would have the anomalous result of depriving the Tax Court of its jurisdiction to review claims for relief under § 722. Such relief can be sought only by way of a claim for refund (see § 722 (d)), and it is only by reason of § 732 (a) that the Tax Court, whose jurisdiction is otherwise limited to deficiency proceedings, has jurisdiction over claims for refund in such cases. Thus, petitioner's argument requires attributing to Congress an intent not only to broaden appellate review but also to channel § 722 cases into the district courts rather than the Tax Court—in short, a complete turnabout from the specialized procedure deemed necessary by Congress when it specifically dealt with the matter.